FILE COPY

APR 28
CHARLES ELMORE

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1935

No. 859

C. L. ASHTON, et al.,
Petitioners,

vs.

CAMERON COUNTY WATER IMPROVEMENT DISTRICT No. 1,
Respondent.

BRIEF FOR AMICI CURIAE.

STEPHEN W. DOWNEY,
Capital National Bank Building, Sacramento, California,
Attorney for Merced Irrigation District.

HARRY W. HORTON,
El Centro, California,
Attorney for Imperial Irrigation District.

GEORGE HERRINGTON,
Financial Center Building, San Francisco, California,
Attorney for Merced Irrigation District Bondholders' Protective Committee and Imperial Irrigation District Bondholders' Protective Committee.

DOWNEY, BRAND & SEYMOUR,
Capital National Bank Building, Sacramento, California,
HORTON & KIRK,
El Centro, California,
ORRICK, PALMER & DAHLQUIST,
Financial Center Building, San Francisco, California,
Of Counsel.

Subject Index

I. Page

Section 80 of the National Bankruptcy Act is a uniform law on the subject of bankruptcies 7

II.

Section 80 of the National Bankruptcy Act does not invade the sovereign powers of any state nor infringe upon state rights guaranteed by the Tenth Amendment to the Constitution 9

1. Section 80 expressly preserves the "sovereign rights" of the States 9

2. Section 80 in its effective operation is limited to matters over which the "sovereign rights" of States cannot extend 11

III.

If sovereign rights of the State of Texas are invaded by Section 80 of the National Bankruptcy Act the invasion is by consent of the state 14

IV.

The bankruptcy power vested in the Federal Government may be exercised irrespective of sovereign rights of the States 17

A. Bankruptcies 17

B. Interstate commerce 18

C. Power to coin money and to regulate the value thereof 19

D. War power 20

Conclusion 24

Table of Authorities Cited

Pages

Ashwander v. Tennessee Valley Authority, ... U. S. ..., 80 L. ed. (Adv. Op.) 427, 56 S. Ct. 466 17

Baltimore National Bank v. State Commission of Maryland, ... U. S. ..., 80 L. ed. (Adv. Op.) 388, 56 S. Ct. 417 16

Board of Trustees of University of Ill. v. United States, 289 U. S. 48, 77 L. ed. 1025, 53 S. Ct. 509 18

California Statutes, 1935—Extra Session 1934, page 5 2

Campbell v. Alleghany Corp., 75 F. (2d) 947, certiorari denied 296 U. S. ..., 80 L. ed. (Adv. Op.) 104, 56 S. Ct. 92 9

C. C. H.—Bankruptcy Law Service, par. 2802, subpar. .02 4

Cincinnati N. O. & Texas Pac. Railway v. Interstate Commerce Commission, 162 U. S. 184, 40 L. ed. 935, 16 S. Ct. 700 18

Clark v. Barnard, 108 U. S. 436, 2 S. Ct. 878, 27 L. ed. 780 15

33 Columbia Law Review (1933), 913, 914 22

35 Columbia Law Review, p. 434 21

35 Columbia Law Review (1935), pp. 434, 435 13

Constitution of the United States:

- Article I, Section 9, clause 4 21
- Article I, Section 10 ..... 3, 12
- Article I, Section 10, clause 1 23
- Fifth Amendment 9
- Tenth Amendment 17
- Eleventh Amendment 15

Continental Illinois National Bk. & Tr. Co. v. Chicago R. I. & P. Ry. Co., 294 U. S. 648, 55 S. Ct. 595, 79 L. ed. 1110 ..... 8, 23

Fallbrook Irrigation District v. Bradley, 164 U. S. 112, 41 L. ed. 369, 17 S. Ct. 56 2

General and Special Laws of Texas, Regular Session 1935, page 293, chapter 107 14

Gibbons v. Ogden, 9 Wheat. 1, 199 (U. S. 1824) 22

Gunter v. Atlantic Coast Line, 200 U. S. 273, 26 S. Ct. 252, 50 L. ed. 477 15

Page

Hagar v. Reclamation District, 111 U. S. 701, 28 L. ed. 569, 4 S. Ct. 663 2

Hagood v. Southern, 117 U. S. 52, 6 S. Ct. 608, 29 L. ed. 805 15

Hanover National Bank v. Moyses, 186 U. S. 181, 22 S. Ct. 857, 46 L. ed. 1113 8

Hensley v. Reclamation Dist., 121 Cal. 96, 53 Pac. 401 5

Imperial Irrigation District, In re, 10 Fed. Supp. 832 2

Indian Motorcycle Co. v. United States (1931), 283 U. S. 570, 51 S. Ct. 601, 75 L. ed. 1227 21

International Shoe Co. v. Pinkus (1929), 278 U. S. 261, 265, 49 S. Ct. 108, 73 L. ed. 318 23

Interstate Commerce Commission v. Detroit etc. Railway Co., 167 U. S. 633, 42 L. ed. 317, 17 S. Ct. 919 18

Kuback, C. J., v. City of Long Beach, 82 Cal. App. Dec. 452, 48 P. (2d) 181 5

Louisville Joint Stock Land Bank v. Radford, 295 U. S. 555, 79 L. ed. 1593, 55 S. Ct. 854 8

Marra v. San Jacinto & Pleasant Valley Irr. Dist., 131 Fed. 780 5

Massachusetts v. Mellon, 262 U. S. 447, 43 S. Ct. 597, 67 L. ed. 1078 16

McCulloch v. State of Maryland, 4 Wheat. 316, 4 L. ed. 579 22

Metcalf & Eddy v. Mitchell (1926), 269 U. S. 514, 524, 46 S. Ct. 172, 70 L. ed. 384 13

Nevada National Bank v. Poso Irrigation Dist., 140 Cal. 344, 73 Pac. 1056 5

New York v. Irving Trust Co. (1933), 288 U. S. 329, 77 L. ed. 815, 53 S. Ct. 389 17

New York v. United States (1922), 257 U. S. 591, 42 S. Ct. 239, 66 L. ed. 385 19

Norman v. Baltimore & Ohio R. R., 294 U. S. 240, 79 L. ed. 885, 55 S. Ct. 407 19

Norris v. Montezuma, 248 Fed. 369 5

Northern Pacific R. R. Co. v. North Dakota (1919), 250 U. S. 135, 39 S. Ct. 502, 63 L. ed. 897 20

Page

Owensboro v. Owensboro National Bank, 173 U. S. 664, 43 L. ed. 850, 19 S. Ct. 875 16

Pabst Brewing Co. v. Crenshaw, 198 U. S. 17, 25 S. Ct. 552, 49 L. ed. 925 15
People v. Honey Lake Valley Irr. Dist., 77 Cal. App. 367, 246 Pac. 819 5
Perris Irrigation Dist. v. Thompson, 116 Fed. 832 5
Pollock v. The Farmers Loan & Trust Co. (1895), 157 U. S. 429, 584, 15 S. Ct. 673, 39 L. ed. 759 21

Reiman, In re, Fed. Cas. No. 11,673 23
Rialto Irrigation District v. Stovell, 246 Fed. 294 5

South Carolina v. United States, 199 U. S. 437, 50 L. ed. 261, 26 S. Ct. 110 18

Thompson v. Perris Irrigation Dist., 116 Fed. 769 5

Van Huffel v. Harkelrode, 284 U. S. 225, 52 S. Ct. 115, 76 L. ed. 256 17
Vernon's Annotated Revised Civil Statues of Texas, 1935 Supplement, Article 1024 14

Willcuts v. Bunn, 282 U. S. 216, 51 S. Ct. 125, 75 L. ed. 304 13
2 Willoughby Constitutional Law of the United States, 2d Ed., 1929, Sec. 415 21

In the Supreme Court
OF THE
United States

OCTOBER TERM, 1935

No. 859

C. L. ASHTON, et al.,
Petitioners,

vs.

CAMERON COUNTY WATER IMPROVEMENT DISTRICT No. 1,
Respondent.

BRIEF FOR AMICI CURIAE.

Two appeals are pending in the United States Circuit Court of Appeals for the Ninth Circuit from decrees entered under the provisions of Section 80 of the National Bankruptcy Act. Pursuant to these decrees readjustments have been effected as to the bonded indebtedness of the Merced Irrigation District [1] (aggre-

1. C. C. A. 9th Circuit, In re Merced Irrigation District, No. 8165; appeal from the decision of the Hon. George Cosgrave, District Judge; unreported.

gating $16,190,000) and of the Imperial Irrigation District [2] (aggregating $14,250,000) respectively.

Numerous other cases are pending in the United States District Courts for the Northern and Southern Districts of California involving the readjustment of the indebtedness of irrigation districts [3] and reclamation districts [4]—taxing districts, organized under the laws of the State of California.[5] The State Legislature, recognizing the necessity for relief from the burden of indebtedness incurred by these districts, passed an enabling act in effect September 20, 1934 (California Statutes, 1935—Extra Session 1934, page 5)[6] authorizing taxing districts to avail themselves of the provisions of Section 80 of the National Bankruptcy Act. The emergency declaration attached to this Act constitutes a legislative finding of the facts existing in this State which renders essential the exercise by taxing districts of the provisions of the National Bankruptcy Act, viz.:

---

2. C. C. A. 9th Circuit, In re Imperial Irrigation District, No. 7970; appeal from the decision of the Hon. P. J. McCormick, District Judge; reported in *In re Imperial Irrigation District*, 10 Fed. Supp. 832.

3. The California Irrigation District Act under which irrigation districts may be organized in California was sustained in *Fallbrook Irrigation District v. Bradley*, 164 U. S. 112, 41 L. ed. 369, 17 S. Ct. 56.

4. The statutes under which reclamation districts may be organized in California was sustained by the United States Supreme Court in *Hagar v. Reclamation District*, 111 U. S. 701, 28 L. ed. 569, 4 S. Ct. 663.

5. Proceedings are also pending in the District Courts of this Circuit with respect to Plans of Readjustment presented by Banta-Carbona Irrigation District, East Contra Costa Irrigation District, El Dorado Irrigation District, Lindsay-Strathmore Irrigation District, Oroville-Wyandotte Irrigation District, Oakdale Irrigation District, Paradise Irrigation District, Palo Verde Irrigation District, Pescadero Reclamation District No. 2058, San Dieguito Irrigation District, Santa Fe Irrigation District, South San Joaquin Irrigation District, Vista Irrigation District and the Waterford Irrigation District.

Petitions under Section 80 of the National Bankruptcy Act are about to be filed by Beaumont Irrigation District, Corcoran Irrigation District and the Glenn-Colusa Irrigation District.

6. This Act is set forth in Appendix "A" hereof.

"Sec. 13. This act is hereby declared to be an urgency measure within the meaning of section 1 of Article IV of the Constitution, necessary for the immediate preservation of the public peace, health and safety, and shall take effect immediately.

The facts constituting such necessity are as follows: There exist throughout the State of California economic conditions which make it impossible for property owners to pay their taxes and special assessments levied upon real or taxable property. The burden of such taxes and special assessments is so onerous in amount that great delinquencies have occurred in the collection thereof and seriously affect the ability of taxing districts to obtain the revenue necessary to conduct governmental functions and to pay obligations represented by bonds. It is essential that financial relief, as set forth in this act, be immediately afforded to such taxing districts in order to avoid serious impairment of their taxing systems, with consequent crippling of the local governmental functions of the State. This act will aid in accomplishing this necessary result and should therefore go into effect immediately."

Article I, Section 10, of the Federal Constitution providing that no State shall pass any law impairing the obligation of contracts, constitutes an insurmountable bar to State legislative assistance to distressed taxing districts. That the condition in California is not solely a matter of local concern is indicated by the Report of the Congressional Committee which recommended the adoption of Section 80 and by the relief

which has been extended by the Reconstruction Finance Corporation to drainage, levee, irrigation and reclamation districts throughout the United States pursuant to appropriations made by Congress for this purpose.

The purpose and effect of Section 80 are stated in the Report of the House Judiciary Committee, June 7, 1933 (C. C. H.—Bankruptcy Law Service, Par. 2802 Subpar. .02), as follows:

> "The controlling purpose of the bill is to provide a forum where distressed cities, counties, and minor political subdivisions, designated in the bill as 'taxing districts', of their own volition, free from all coercion, may meet with their creditors under the necessary judicial control and assistance in an effort to effect an adjustment of their financial matters upon a plan deemed mutually advantageous. If a plan is agreed upon by the taxing district and its creditors holding two-thirds in amount of the claims of each class of indebtedness, and if the court is satisfied that the plan is workable and equitable, it may confirm the plan, and the minority creditors are bound thereby."

The purpose of the legislation is to subordinate the demands of the minority creditors to the wishes of the majority, to force a recalcitrant minority to accept that which is for their own best interests and to enable governmental agencies to function and to continue to discharge their governmental obligations.

While the Bankruptcy Act is designated primarily for the relief of debtors, experience has proved that only through the medium of Section 80 can the holders

of bonds and other securities of distressed taxing districts secure an adequate remedy for the effective readjustment of their own defaulted securities. Prior to the enactment of Section 80 the bondholders found that the exercise of their strict legal remedies aggravated rather than cured the condition of default. Increased or pyramided tax levies upon land which did not have the capacity to pay the original indebtedness inevitably forced further defaults. Voluntary plans of readjustment were never effective against the usual minority groups. The physical assets of a public taxing district —at least in California—cannot be taken under execution and public funds cannot be seized by garnishment or attachment.[7] The sole source from which the indebtedness of the taxing district may be paid is by the collection of taxes levied upon the land.[8] The economic law—when taxes exceed the value of the land they cannot be collected—has brought disaster to the bondholders, as well as ruin to the districts, the operation and maintenance of whose improvement works for supplying water or providing flood control or reclamation are likewise dependent upon the collection of taxes levied and assessed upon the lands. Minority bondholders by compelling, as they have the legal right to do, the annual assessment of additional taxes upon the

7. *Rialto Irrigation District v. Stovell*, 246 Fed. 294;
Norris v. Montezuma, 248 Fed. 369;
C. J. Kuback v. City of Long Beach, 82 Cal. App. Dec. 452. 48 P. (2d) 181;
People v. Honey Lake Valley Irr. Dist., 77 Cal. App. 367, 246 Pac. 819;
Hensley v. Reclamation Dist., 121 Cal. 96, 53 Pac. 401.

8. *Nevada National Bank v. Poso Irrigation Dist.*, 140 Cal. 344, 73 Pac. 1056;
Thompson v. Perris Irrigation Dist., 116 Fed. 769;
Perris Irrigation Dist. v. Thompson, 116 Fed. 832;
Marra v. San Jacinto & Pleasant Valley Irr. Dist., 131 Fed. 780.

land to meet delinquencies in the payment of district indebtedness have inevitably brought about a complete breakdown in the tax collecting ability of the districts, thereby depriving all of the security holders of their sole source of income applicable to the payment of the district indebtedness. The result is that large areas of land in California have been forced off of the tax roll and while in public ownership are incapable of producing revenues. Unless plans of readjustment and refinancing can be made effective under the provisions of Section 80 of the National Bankruptcy Act, it is only a question of time, with respect to many of these districts, when they will become wholly unable to produce any substantial amount of revenue for the payment of their bonded debts. The same reasons which impelled the Congress to enact Section 77, relating to reorganization of railroads, and Section 77B, relating to reorganization of corporations, apply with equal force to taxing districts. Defaults by taxing districts in substantially all cases can be traced to the same cause —inability to collect taxes levied upon the lands in the district due to the overwhelming burden of the tax necessary to meet the indebtedness. Readjustments and plans of reorganization all involve the essential element of concessions by the bondholder, either (a) by postponing the time of payment of the indebtedness, or (b) by scaling the amount of the indebtedness to a point within the capacity of the land to pay.

The plan of readjustment of the Imperial Irrigation District essentially involved postponement of the time of payment of serial bonds over a fifty-year period, the

postponement being accomplished by exchange of refunding bonds maturing January 1, 1983 for substantially all of the then outstanding serial bonds.

The plan of readjustment of the Merced Irrigation District essentially involved a cash payment of $515.01 per $1000 of outstanding bonds (reducing the total indebtedness by approximately 50% and the interest rates from 5½% and 6% to 4%), the funds being derived through a loan to the District from the Reconstruction Finance Corporation for this purpose.

In both cases the readjustments were assented to by the holders of approximately 90% of the outstanding bonds before the respective District Courts were asked to determine that the plans were "fair, equitable and for the best interest of creditors."

We submit that Section 80 of the National Bankruptcy Act is a law on the subject of bankruptcies passed under the express power conferred by the States upon the Congress of the United States and is therefore a law directly authorized by the Constitution and is not in violation thereof.

I.

SECTION 80 OF THE NATIONAL BANKRUPTCY ACT IS A UNIFORM LAW ON THE SUBJECT OF BANKRUPTCIES.

Territorial uniformity obviously exists by the very terms of the Act which is applicable to taxing districts of every kind or nature, wheresoever located through-

out the United States.[9] The section essentially authorizes a composition of creditors through a "plan of readjustment" approved by the Court and assented to both by the taxing district and by more than the usual majority of creditors. No taxing district can be forced to accept a plan of readjustment. No creditor is bound until a sufficient majority accepts the composition. A composition of creditors is clearly a law on the subject of bankruptcy, and the constitutional grant of power does not require the surrender of the debtor's assets as a condition to such composition.

Continental Illinois National Bk. & Tr. Co. v. Chicago R. I. & P. Ry. Co., 294 U. S. 648, 55 S. Ct. 595, 79 L. ed. 1110.

No arbitrary plan is prescribed by the statute as a condition precedent to any proposed plan of readjustment and the coercive and arbitrary features of the legislation condemned by this Court in

Louisville Joint Stock Land Bank v. Radford, 295 U. S. 555, 79 L. ed. 1593, 55 S. Ct. 854,

are wholly absent.[10] On the contrary, no plan can be confirmed until a Court of the United States has found

9. *Hanover National Bank v. Moyses*, 186 U. S. 181, 22 S. Ct. 857, 46 L. ed. 1113.

10. In a footnote to this case this Court said:
"The principle of composition was first applied to the interests of secured creditors in their security, by section 74, added to the Bankruptcy Act, by Act of March 3, 1933, c. 204, Sec. 1, 47 Stat. 1467, see 11 USCA Sec. 202 (individual debtors); by section 75, Act of March 3, 1933, c. 204, Sec. 1, 47 Stat. 1470, see 11 USCA Sec. 203 (agricultural compositions); by section 77, Act of March 3, 1933, c. 204, Sec. 1, 47 Stat. 1474, 11 USCA Sec. 205 (railroads engaged in interstate commerce); by section 77B, Act of June 7, 1934, c. 424, Sec. 1, 48 Stat. 912, 11 USCA Sec. 207 (corporations); *and by section 80, as added by Act of May 24, 1934, c. 345, 48 Stat. 798, 11 USCA Sec. 303 (public debtors)*. The constitutionality of such provision in section 74 was considered in *Re Landquist* (C. C. A.), 70 F. (2d) 929, 933" (italics ours).

that it is "*fair, equitable and for the best interests of the creditors, and does not discriminate unfairly in favor of any class of creditors,*" and further that the plan has been accepted and approved by both the requisite number of creditors and by the taxing district, and further that the "*offer of the plan and its acceptance are in good faith.*"

Section 80 therefore satisfies the due process clause of the Fifth Amendment of the Constitution by the provision for voluntary consent of all parties to the composition and by the further requirement of a hearing and of findings by the trial Court on the fairness of the proposed composition before it can be made binding upon the dissenters.[11]

II.

SECTION 80 OF THE NATIONAL BANKRUPTCY ACT DOES NOT INVADE THE SOVEREIGN POWERS OF ANY STATE NOR INFRINGE UPON STATE RIGHTS GUARANTEED BY THE TENTH AMENDMENT TO THE CONSTITUTION.

1. Section 80 expressly preserves the "sovereign rights" of the States.

Section 80 confers a *limited* jurisdiction upon the United States Courts in Bankruptcy for the purpose of enabling a taxing district to secure a discharge from debts and liabilities dealt with in the plan of readjustment and for the purpose of making the plan binding upon all creditors affected thereby. Jurisdiction can only be acquired over taxing districts which are unable

11. *Campbell v. Alleghany Corp.*, 75 F. (2d) 947; certiorari denied 296 U. S. ..., 80 L. ed. (Adv. Op.) 104, 56 S. Ct. 92.

to pay their debts as they mature. The plan of readjustment which the Court is authorized to confirm must include provisions modifying or altering the *rights of creditors* of the taxing district. No plan of readjustment can be confirmed until the trial Court is satisfied that the *"taxing district is authorized by law, upon confirmation of the plan, to take all action necessary to carry out the plan."* In the exercise of this limited jurisdiction the sovereign power of the State is protected and safeguarded by the provisions of Section 80, which first: reserves to the State its governmental and political powers over its taxing districts; second: requires the approval of State fiscal agencies, if any, to any proceedings instituted under the section by State taxing districts; third: prohibits the Federal Court from interfering with the governmental or political powers of taxing districts; and fourth: protects the political and governmental functions of a taxing district by excepting from the definition of the term "creditors" all claims "for salaries and wages of officers and employees of the taxing district." (National Bankruptcy Act, Sec. 80, subpar. (b).)

> "Nothing contained in this chapter shall be construed to limit or impair the power of any State to control, by legislation or otherwise, any political subdivision thereof in the exercise of its political or governmental powers, including expenditures therefor, and including the power to require the approval by any governmental agency of the State of the filing of any petition hereunder and of any plan of readjustment, and whenever there shall exist or shall hereafter be created under the law of any State any agency of such

State authorized to exercise supervision or control over the fiscal affairs of all or any political subdivisions thereof, and whenever such agency has assumed such supervision or control over any political subdivision, then no petition of such political subdivision may be received hereunder unless accompanied by the written approval of such agency, and no plan of readjustment shall be put into temporary effect or finally confirmed without the written approval of such agency of such plans." (National Bankruptcy Act, Sec. 80, subpar. (k).)

"* * * but (11) shall not, by any order or decree, in the proceeding or otherwise, interfere with (a) any of the political or governmental powers of the taxing district, or (b) any of the property or revenues of the taxing district necessary in the opinion of the judge for essential governmental purposes, or (c) any income-producing property, unless the plan of readjustment so provides." (National Bankruptcy Act, Sec. 80, subpar. (c).)

2. Section 80 in its effective operation is limited to matters over which the "sovereign rights" of States cannot extend.

In its effective operation Section 80 merely confirms to taxing districts the accomplishment of powers conferred upon them by the States. The sovereign power of the State extends to the creation of indebtedness by taxing districts and the payment of that indebtedness by taxes upon the taxable property in the district. The sovereign power of the State cannot extend to the alteration, compromise or adjustment of indebtedness once outstanding and in the hands of private holders—at least against their will—for the States are forbidden

by Section 10 of Article I of the Constitution, to impair the obligation of a contract lawfully created. There is no such limitation upon the authority of the Federal Government. The relief to taxing districts under Section 80 follows an express grant of authority to Congress to pass laws on the subject of bankruptcies and is, therefore, incidental in its operation to the sovereignty of the State which authorized the creation of the indebtedness to be readjusted.

Section 80 operates directly upon the rights of *creditors*—a field of action forbidden to the States. Against the taxing district it operates only to discharge debts readjusted under the plan *approved jointly by the creditors and the district and confirmed by the Federal Court.* In a field where no "state sovereignty" exists, it cannot be said to be "impaired" by a law the power to enact which is vested exclusively in Congress. In the cases which have been decided by this Court a clear distinction has been made between the encroachment upon what is sometimes referred to as sovereign, governmental or political powers which are attributes of sovereignty itself and what may be called the other functions of the governmental entity. These decisions deal almost entirely with tax questions where it is conceded that both the National Government and the State have co-ordinate powers. Even in this class of cases, however, taxes have been repeatedly upheld notwithstanding that they relate to or concern governmental agencies, so long as they do not impair or impede the exercise of sovereign or governmental rights. There is nothing in Section 80 which can be said to substan-

tially burden or interfere with any of the governmental powers of the taxing agencies.

In *Willcuts v. Bunn*, 282 U. S. 216, 51 S. Ct. 125, 75 L. ed. 304, where a Federal income tax on profits resulting from resale of municipal bonds was upheld, this Court said (page 230):

> "* * * No facts as to actual consequences are brought to our attention showing any appreciable burden upon the state's borrowing power."

In another case in which the right of the Federal Government to tax the salary of an individual employed as a consulting engineer by a State was upheld it was stated that:

> *"The extent of the exemption must finally depend upon the effect of the tax upon the functions of the government alleged to be affected by it."*
>
> *Metcalf & Eddy v. Mitchell* (1926), 269 U. S. 514, 524, 46 S. Ct. 172, 70 L. ed. 384,

and see

> 35 *Columbia Law Review* (1935), pp. 434, 435.

It certainly cannot be held that the readjustment of municipal obligations is a substantial burden on or interference with the governmental functions of the State, within the line of cases just referred to. A favorable debt readjustment would appear to foster effective governmental operation rather than to impair it. The argument that such a procedure would impair the borrowing power of municipalities overlooks the fact that under present chaotic business conditions, a creditor's right to full reimbursement is purely

theoretical. A readjustment of the debt burden to a point where satisfaction of existing bond obligations becomes presently possible would present a clear slate for future financing.

III.

IF SOVEREIGN RIGHTS OF THE STATE OF TEXAS ARE INVADED BY SECTION 80 OF THE NATIONAL BANKRUPTCY ACT THE INVASION IS BY CONSENT OF THE STATE.

Assuming that the State sovereignty is invaded by Section 80 of the National Bankruptcy Act, the invasion in the case before the Court is by consent of the State of Texas as evidenced by its enabling act (General and Special Laws of Texas, Regular Session 1935, page 293, Chap. 107; Vernon's Annotated Revised Civil Statutes of Texas, 1935 Supplement Article 1024).

The California Statute set forth in the Appendix hereof likewise constitutes a consent by the State of California to whatever impairment of its "sovereign rights" may be brought about by the institution of proceedings under Section 80 by taxing districts organized under the laws of this State. The doctrine of sovereign rights includes the right of waiver by the "sovereign". Section 80 of the National Bankruptcy Act is not compulsory. It extends to taxing districts a privilege accorded to other debtors by the Bankruptcy Act of which they may or may not elect to avail themselves.

Despite direct prohibition against the entertainment by the Federal Courts of suits brought by individuals against States (Eleventh Amendment) it is well settled that a State may waive its immunity and sovereignty by voluntary appearance in such an action.

Clark v. Barnard, 108 U. S. 436, 2 S. Ct. 878, 27 L. ed. 780;

Gunter v. Atlantic Coast Line, 200 U. S. 273, 26 S. Ct. 252, 50 L. ed. 477;

Hagood v. Southern, 117 U. S. 52, 6 S. Ct. 608, 29 L. ed. 805.

These decisions involve a direct constitutional prohibition against the exercise of Federal jurisdiction but it is nevertheless held such jurisdiction attaches in any case in which the State directly or indirectly waives its sovereign immunity.

It would seem clear that either the State or the Federal Government may waive their respective sovereignties and consent to legislation which without such consent would be unconstitutional. Thus, State legislation taking advantage of the consent of Congress with reference to regulations concerning intoxicating liquor when imported into a State, has been held constitutional.

Pabst Brewing Co. v. Crenshaw, 198 U. S. 17, 25 S. Ct. 552, 49 L. ed. 925.

If the amendment transgresses rights reserved to the States, the consent on the part of the State is a waiver thereof. The United States may waive its own sovereign immunity from taxation by the States.

In *Baltimore National Bank v. State Commission of Maryland,* ..... U. S. ....., 80 L. ed. (Adv. Op.) 388, 56 S. Ct. 417, holding that national bank shares owned by the Reconstruction Finance Corporation may be taxed, this Court says:

> "* * * We assume, though without deciding even by indirection, that within M'Culloch v. Maryland, 4 Wheat. 316, 4 L. ed. 579, a corporation so conceived and operated is an instrumentality of government without distinction in that regard between one activity and another. *Even on that assumption taxation by state or municipality may overpass the usual limits if the consent of the United States has removed the barriers or lowered them.*" (Italics ours.)
>
> *Owensboro v. Owensboro National Bank,* 173 U. S. 664, 43 L. ed. 850, 19 S. Ct. 875.

If Section 80 was enacted with the ulterior purpose of tempting the States to yield their sovereignty, that purpose may be effectively frustrated by the simple expedient of not yielding.

> *Massachusetts v. Mellon,* 262 U. S. 447, 43 S. Ct. 597, 67 L. ed. 1078.

IV.

THE BANKRUPTCY POWER VESTED IN THE FEDERAL GOVERNMENT MAY BE EXERCISED IRRESPECTIVE OF SOVEREIGN RIGHTS OF THE STATES.

To the extent that powers are expressly conferred upon the Federal Government the Tenth Amendment of the Constitution is wholly inapplicable.

Ashwander v. Tennessee Valley Authority, ... U. S. ....., 80 L. ed. (Adv. Op.) 427, 56 S. Ct. 466.

It has been held many times by this Court that the sovereign rights and powers of the States are subject and subordinate to and need not be considered in connection with the regulations of Congress in the undoubted exercise of its war power, the power to coin money and fix the value thereof, power over interstate commerce, and bankruptcy itself.

A. Bankruptcies.

The sovereign right of States to levy taxes upon property within their territorial jurisdictions is subject to the operation of the Bankruptcy Act. Property administered by a Federal Court in bankruptcy may be sold free and clear of the lien of a State tax.

Van Huffel v. Harkelrode, 284 U. S. 225, 52 S. Ct. 115, 76 L. ed. 256.

When a State is a creditor of a bankrupt it must file its claim within the time provided in the Bankruptcy Act. If the State's claim is not on file within that time it cannot be enforced and the bankrupt's discharge will be a release therefrom.

In *New York v. Irving Trust Co.* (1933), 288 U. S. 329, 77 L. ed. 815, 53 S. Ct. 389, it was said (page 333):

"If a state desires to participate in the assets of a bankrupt, she must submit to *appropriate requirements by the controlling power*" (Congress). (Italics ours.)

B. Interstate commerce.

Railroads owned and operated by States in the exercise of their sovereign powers are subject to the jurisdiction of the Interstate Commerce Commission and to such rates as may be enforced by an instrumentality of the United States acting under an authority of Congress to regulate interstate commerce.

Cincinnati N. O. & Texas Pac. Railway v. Interstate Commerce Commission, 162 U. S. 184, 40 L. ed. 935, 16 S. Ct. 700;

Interstate Commerce Commission v. Detroit etc. Railway Co., 167 U. S. 633, 42 L. ed. 317, 17 S. Ct. 919; and

South Carolina v. United States, 199 U. S. 437, 50 L. ed. 261, 26 S. Ct. 110.

Furthermore State legislation affecting interstate commerce must yield to subsequent acts of Congress enacted under the sole and exclusive right to regulate interstate commerce conferred upon Congress by the Federal Constitution.

In *Board of Trustees of University of Ill. v. United States*, 289 U. S. 48, 77 L. ed. 1025, 53 S. Ct. 509, this Court said at page 57 of 289 U. S.:

"The principle of duality in our system of government does not touch the authority of the Congress in the regulation of foreign commerce."

In the case of *New York v. United States* (1922), 257 U. S. 591, 42 S. Ct. 239, 66 L. ed. 385, it was held that a ruling of the Interstate Commerce Commission increasing the rates to be charged by certain railroads doing business in the State of New York was constitutional irrespective of the fact that the State of New York had previously entered into express contracts with such railroads by which the latter were bound to charge much lower rates for service performed within the State.

C. Power to coin money and to regulate the value thereof.

Acting under its express authority Congress may strike down contracts of sovereign States and their political subdivisions by prohibiting and rendering invalid the obligation to pay in gold coin of the United States debts previously incurred.

In *Norman v. Baltimore & Ohio R. R.*, 294 U. S. 240, 79 L. ed. 885, 55 S. Ct. 407, it was said:

> "The instant cases involve contracts between private parties, but the question necessarily relates as well to the contracts or obligations of States and municipalities, or of their political subdivision, that is, to such engagements as are within the reach of the applicable national power." (294 U. S. 306.)
>
> * * * * * * *
>
> "If the gold clauses now before us interfere with the policy of the Congress in the exercise of that authority they cannot stand." (294 U. S. 311.)
>
> * * * * * * *

"And if the Congress would have that power in the absence of gold clauses, principles beyond dispute compel the conclusion that private parties, or States or municipalities, by making such contracts could not prevent or embarrass its exercise. In that view of the import of the gold clauses, their obstructive character is clear." (294 U. S. 313, 314.)

* * * * * * *

"The contention that these gold clauses are valid contracts and cannot be struck down proceeds upon the assumption that private parties, and States and municipalities, may make and enforce contracts which may limit that authority. Dismissing t' [illegible]enable assumption, the facts must be faced. We think that it is clearly shown that these clauses interfere with the exertion of the power granted to the Congress and certainly it is not established that the Congress arbitrarily or capriciously decided that such an interference existed." (294 U. S. 316.)

D. War Power.

This Court has held that under the "war power" Congress is authorized to regulate even *intrastate* commerce. (See *Northern Pacific R. R. Co. v. North Dakota* (1919), 250 U. S. 135, 39 S. Ct. 502, 63 L. ed. 897.)

State rights must yield to the exercise of an express power granted to Congress by the terms of the Constitution. The theory of dual sovereignty is one which is not expressed in the Constitution but is only to be implied from its terms. It is therefore a doctrine arising by implication which must yield in every instance if it

conflicts with the power expressly granted, reserved or limited by the terms of the Constitution.

We submit that the bankruptcy power should be classified with those other powers of the National Government whose plenary nature renders them invulnerable to objections based on State sovereignty. (35 *Columbia Law Review*, p. 434.)

One of the primary reasons behind the decisions of this Court to the effect that the question of State sovereignty need not be considered in the exercise by Congress of its commerce, currency and military powers is the fact that uniformity of legislation with respect to such matters is essential. (See 2 *Willoughby Constitutional Law of the United States*, 2d Ed., 1929, Sec. 415.) It is obvious that uniformity of bankruptcy legislation is similarly requisite, and, indeed, such uniformity is expressly enjoined by the Constitution (Art. I, Sec. 9, Clause 4).

It is true that the exercise by Congress of one of its primary powers, i. e., taxation, has been on several occasions restricted by this Court in order to prevent Congress from completely impairing or destroying the sovereignty of the several States.

See:

Indian Motorcycle Co. v. United States (1931), 283 U. S. 570, 51 S. Ct. 601, 75 L. ed. 1227;

Pollock v. The Farmers Loan & Trust Co. (1895), 157 U. S. 429, 584, 15 S. Ct. 673, 39 L. ed. 759.

However, from the very nature of taxation, it is obvious that the power to tax was not entrusted to the Fed-

eral Government to enable it to impose a uniform system of taxation on the nation. Taxation is a power inherent in a sovereign, providing the necessary wherewithal to its existence, and necessarily was made available equally to the States and to the Federal Government independently of its exercise by one or the other. (*Gibbons v. Ogden,* 9 Wheat. 1, 199 (U. S. 1824).) In *McCulloch v. State of Maryland,* 4 Wheat. 316, 4 L. ed. 579, it is said (4 L. ed. 606):

> "That the power of taxation is one of vital importance; that it is retained by the states; that it is not abridged by the grant of a similar power to the government of the Union; that it is to be concurrently exercised by the two governments; are truths which have never been denied."

This is said to be the only case in which a power granted to Congress expressly by the Constitution, and not expressly limited therein, has been limited by the Courts in order to protect the sovereignty of the States. See:

33 *Columbia Law Review* (1933), 913, 914.

There is no similarity between the power of taxation and the bankruptcy power. Congress has been restricted to some extent in the exercise of its taxing power because, as has been said, the very nature of taxation, furnishing, as it does, the means of supplying a sovereign with the necessary wherewithal for existence, requires that in the dual system of government the power of each sovereign to tax must not be fettered by the other sovereign. However, a consideration of the bankruptcy power reveals that this element is completely lacking therein. The "contracts" clause of the

Constitution (Art. I, Sec. 10, Clause 1) specifically prohibits the States from enacting bankruptcy legislation by forbidding them the right to impair the obligations of contracts. Therefore, the whole basis for this particular distinction between the restricted tax power and the plenary currency, commerce and military powers is non-existent in the case of bankruptcy power.

A further reason for classifying the bankruptcy power with the commerce, currency and military powers, rather than with the taxing power, is the very necessity for uniformity which is required by the bankruptcy clause of the Constitution and which, as has been stated, is the primary basis for holding the commerce, currency and military powers of Congress to be plenary and invulnerable to objections based on State sovereignty.

In addition, it has been previously said by this Court that the bankruptcy power of Congress is "unrestricted and paramount". (*International Shoe Co. v. Pinkus* (1929), 278 U. S. 261, 265, 49 S. Ct. 108, 73 L. ed. 318.) In the case of *In re Reiman,* Fed. Case No. 11,673, which is the leading case on compositions in bankruptcy and which was cited with approval in *Continental Illinois Nat. Bank & Trust Co. v. Chicago R. I. & P. Ry. Co.,* 294 U. S. 648, 79 L. ed. 1110, 55 S. Ct. 595, it is said:

> "* * * that the power to establish laws on 'the subject of bankruptcies' gives an authority over the subject, that is not restricted by the limitation found in the English Statutes in force when the Constitution was adopted. *The power given must,*

indeed, be held to be general, unlimited and unrestricted over the subject." (Italics ours.)

CONCLUSION.

In conclusion we submit that Section 80 of the National Bankruptcy Act is a valid law on the subject of bankruptcies; that it provides for a voluntary composition of creditors and that it does not in any respect impair the sovereign powers reserved to the States.

Dated, San Francisco, California,
April 22, 1936.

Respectfully submitted,
STEPHEN W. DOWNEY,
Attorney for Merced Irrigation District.
HARRY W. HORTON,
Attorney for Imperial Irrigation District.
GEORGE HERRINGTON,
Attorney for Merced Irrigation District Bondholders' Protective Committee and Imperial Irrigation District Bondholders' Protective Committee.

DOWNEY, BRAND & SEYMOUR,
HORTON & KIRK,
ORRICK, PALMER & DAHLQUIST,
Of Counsel.

(Appendix Follows.)